



One asset class, many strategies: a selection framework for private debt

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“Private debt encompasses a spectrum that runs from infrastructure and real estate loans to asset-backed finance, through opportunistic and distressed credit strategies.”

Private debt is an increasingly established part of strategic asset allocations, but there is more to this than private credit.

Key takeaways:

- **Private debt is not a single strategy:** it spans a plethora of sub-strategies from private credit to real asset debt, asset-backed finance, and beyond. Each has distinct risk and return characteristics, but many investors access only a subset of the wider opportunity set.
- **Returns in private debt are built differently by strategy:** understanding that decomposition changes how to size, position and stress-test each allocation.
- **Strategy selection requires a framework, not a shortlist:** we propose five diagnostic questions that offer investors a structured basis for assessing which private debt strategies could belong in their portfolio.

Most institutional investors who hold private debt are, in practice, holding private credit, more specifically senior secured loans to mid-market corporates. That exposure has served them well. But it represents one corner of a much broader opportunity set, and for many portfolios it is now the entirety of their private debt allocation, perhaps by default rather than by design.

Private debt encompasses a spectrum that runs from infrastructure and real estate loans to asset-backed finance (for example secured against royalties or aircraft cash flows), through to opportunistic and distressed credit strategies. These sub-strategies differ not just in the borrowers they serve, but in their risk and return profiles, their sensitivity to rates and economic cycles, and the portfolio objectives they can realistically address.

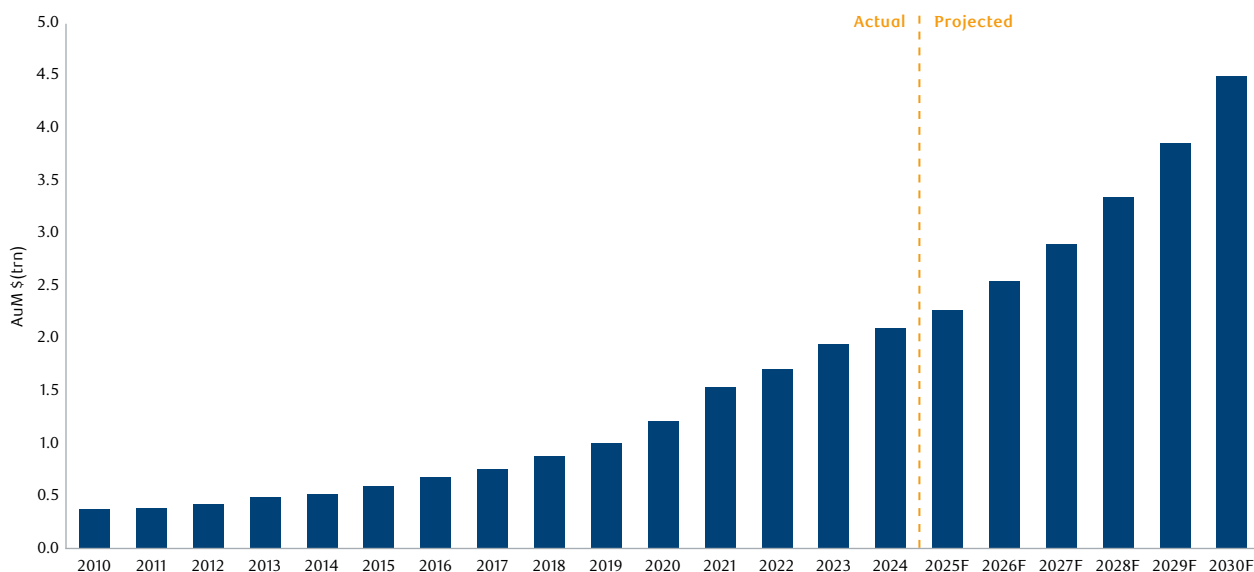
A pension fund seeking long-duration income, an insurer managing Solvency II capital efficiency, and an endowment targeting return enhancement each have a different answer to the question of which private debt strategies belong in their portfolio.

In this paper we make the case for allocating to it more deliberately, mapping the range of private debt strategies, explaining what drives returns, and proposing a practical framework for assessing which strategies belong in which portfolios. The aim is not to make the case for private debt, but to help investors navigate the wide range of sub-strategies more purposefully.

Private debt has grown too large to ignore – and it’s still growing

Asset class wide private debt AUM is now around US\$2 trillion, up from around \$380 billion in 2010. And this is projected to reach close to \$4.5 trillion by 2030, according to data from Preqin.

Private debt AUM projected growth (\$trn)



Source: Preqin, RBC Global Asset Management, data as at October 2025. Projected figures are estimates and subject to change.

Private debt’s growth was primarily driven by private credit amid banks’ retreat from middle-market corporate lending. Meanwhile, the era of low interest rates that followed the global financial crisis sparked demand for private credit. Institutional investors found private debt’s combination of yield premium, inflation-adjusted contractual income, and diversification from public markets increasingly compelling. That demand has proven durable across rate environments, reflecting structural portfolio needs.

Understanding the sources of increasing risk in private credit today

Three years of comparatively more elevated rates have shifted the operating environment for private credit in ways that weren’t anticipated when capital flooded into the strategy. Interest coverage ratios in leveraged middle-market credits have compressed, and the same floating rate structure that boosted investor income has simultaneously squeezed borrower margins. Default rates, while not alarming in absolute terms, are rising steadily from the historic lows seen in 2021–2022, and the mix of credits showing stress is broadening. For portfolios with meaningful legacy vintage exposure from 2020–2022, this is not an abstract risk.

There is also structural pressure that compounds the cyclical dynamic. The volume of institutional capital that has moved into private credit over the past decade has eroded the reward. Spreads in senior secured direct lending have narrowed meaningfully, and the illiquidity and complexity premium that once made direct lending’s headline yield so distinctive has been partially arbitrated away.

In the US, revisions to bank capital requirements are enabling large banks to compete more aggressively in leveraged lending, adding further pressure to a corner of the market where spreads are already compressed.

In Europe, by contrast, so called Basel IV’s tightening output floor continues to constrain bank appetite, sustaining private credit’s structural advantage in that market.

In parts of the market, investors are being asked to accept more risk for less compensation than was available even two years ago.

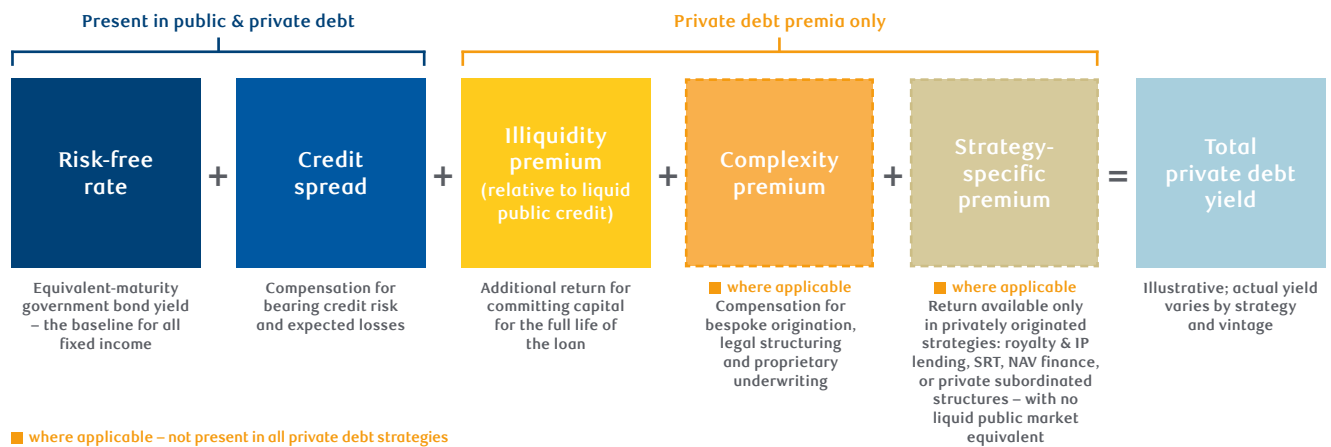
Against this backdrop, the case for looking beyond private credit, towards private debt strategies with different return drivers, different borrower universes, and different structural protections, is in our view stronger than it has been at any point in the asset class’s modern history.

The sources of return in private debt

While private debt is far from a homogeneous asset class, what unites the full range of sub-strategies is not the type of borrower but the nature of that relationship. Private debt is financing outside public markets, and typically arranged directly between lender and borrower, without the standardisation or price transparency that public issuance requires.

It is helpful to decompose total yield to illustrate the similarities and differences versus public debt. Like in public markets, total yield is composed of a risk-free rate plus a credit spread premium. For private debt there is an additional illiquidity premium, and depending on the strategy and market environment, other risk premia too. The chart below illustrates how these components combine. Together they have historically offered an attractive premium over comparable public credit instruments; not as an anomaly or a free lunch, but as the price of genuine structural differences between private and public lending.

An illustration of private credit yield drivers



Source: RBC Global Asset Management, illustrative.

Components are not to scale. Complexity and strategy-specific premia apply where relevant to the sub-strategy.

Understanding the risks in private debt

Private debt strategies can be grouped in various ways, and the underlying drivers of risk and return differ materially across sub-strategies. Understanding those differences, not just at the asset class level, but at the level of what can actually go wrong in each structure, is key to sizing and managing allocations.

Additional risks pertinent to private debt

Liquidity and refinancing dependency: unlike public markets, private debt offers no secondary price discovery and limited exit mechanisms. Investors typically commit for the life of the loan, but the liquidity dependency runs both ways: borrowers in many strategies also rely on functioning refinancing markets to roll at maturity. Where that access closes, as it did for some real estate credits in 2022–2023, liquidity can quickly dry up. NAV and fund finance strategies carry additional exposure because of their dependency on underlying portfolio valuations. In contrast to actively managed publicly listed credit, the inability to trade positions limits the ability of managers to adjust portfolios in the face of higher volatility.

Valuation and transparency: private debt instruments are often valued by model rather than observable market price. This creates two related risks: mark-to-model smoothing can spread losses across multiple reporting periods, creating a misleading picture of stability, and the opacity of underlying holdings makes it difficult to independently verify whether reported valuations reflect current conditions. Both effects tend to be most acute, and most consequential precisely during periods of market dislocation, potentially delaying risk management responses.

Risks common to public and private debt

There are of course various other risks to be aware of, and the following are typically common to both public and private debt, again depending on the underlying sub-strategy.

Repayment risk: this is about how the loan is repaid, from cash flows, asset values or both. Understanding which repayment mechanism a strategy relies on, and how resilient that mechanism is under stress, is the starting point for any meaningful risk assessment and scenario analysis.

Structural amplification mechanisms: credit structures redistribute and amplify risk in ways that underlying quality alone may not reveal. Leverage increases return sensitivity to small movements in asset values; tranching and subordination concentrate first-loss risk in junior positions while providing apparent protection to senior holders. As a result, a modest portfolio deterioration can generate outsized losses for specific holders. Capital structure position is equally as important as credit assessment.

Correlation and systemic stress: credit strategies may appear well-diversified in normal market conditions, but that diversification can deteriorate sharply in episodes of systemic stress. When risk-off pressure dominates, strategy-specific distinctions matter less than common institutional exposures: simultaneous redemption pressure, capital constraints, and the withdrawal of liquidity across markets.

Stress correlations are typically higher than normalised estimates suggest, and portfolio construction should account for this. For private debt, historical correlation data may understate true correlation, as model-based and appraisal-driven valuations smooth reported returns (a limitation addressed in the valuation section above).

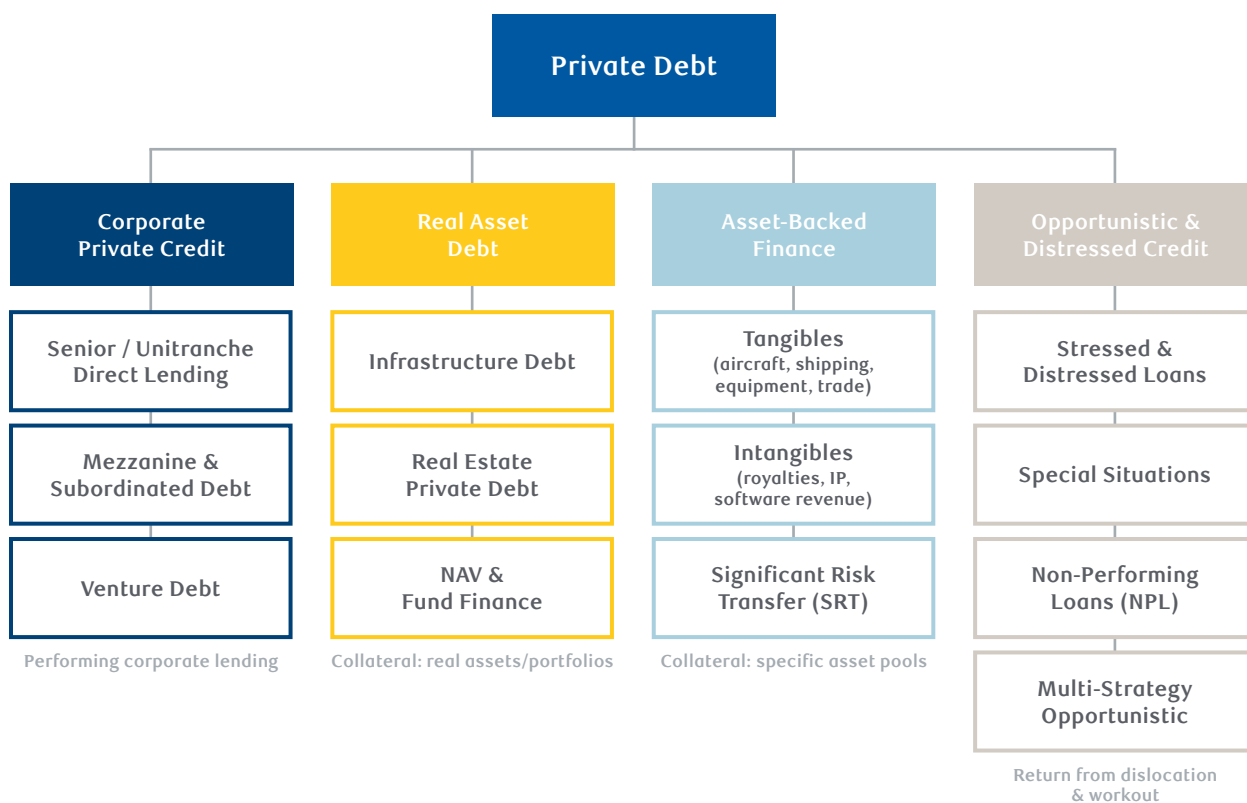
“For private debt, historical correlation data may understate true correlation, as model-based and appraisal-driven valuations smooth reported returns.”

Which strategies form part of private debt?

Private debt encompasses a wide spectrum of lending activity, from loans to privately owned businesses, to financing secured against real assets, infrastructure, or pools of financial assets.

Taxonomies vary across the industry; the framework below offers one coherent way to map the full opportunity set. There are, in essence, four sub-strategies within private debt:

Private Debt – Strategy Taxonomy



Source: RBC Global Asset Management, May 2026.
For illustrative purposes only. Not investment advice.

Private debt has grown too large to ignore – and it's still growing

Q1. What portfolio role is the private debt strategy intended to serve?

Consider the portfolio objective for the allocation; income, diversification, liability matching, liquidity solutions, or more opportunistic returns. Review the investment horizon and deployment requirements? Assess the degree of overlap with existing private debt exposures; is the goal to complement what is already held, or to diversify away from it?

Q2. What are the primary underlying risks that drive the strategy?

In private credit this will typically include corporate earnings risk, default risk and leverage sensitivity. Infrastructure debt involves asset cash flow risk and duration sensitivity. Asset-backed strategies introduce collateral performance risk and, for more esoteric structures, the additional complexity of valuing non-standard assets. Understanding the specific risk that drives repayment, cash flow, collateral, or a combination, is the foundation of any meaningful assessment.

Q3. How might the strategy perform during times of stress, in terms of correlation, liquidity freezes and valuation pressure?

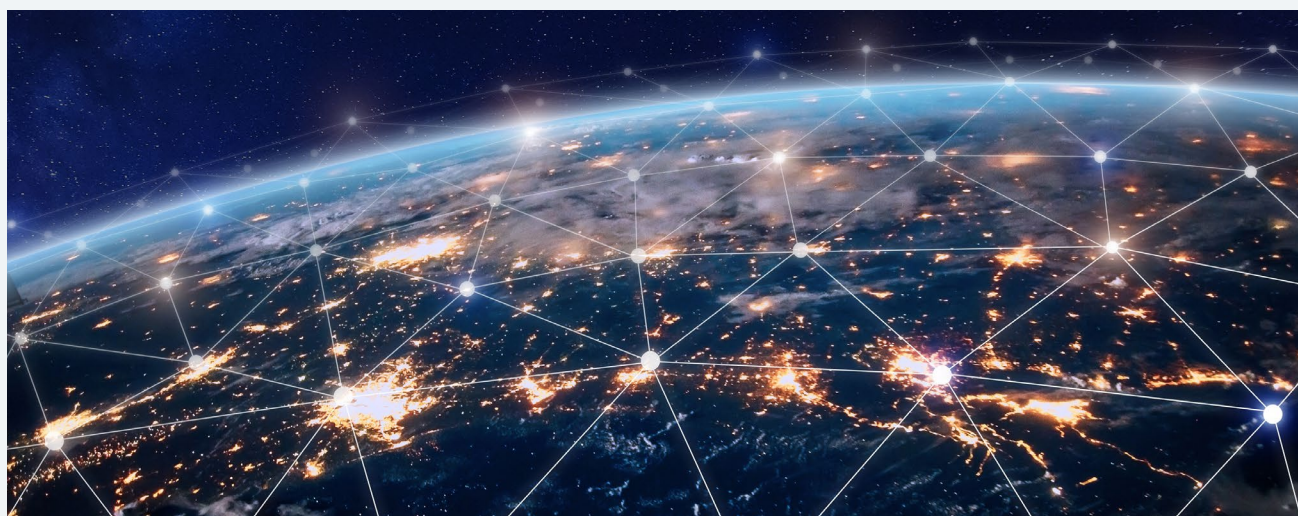
Strategies backed by contractual cash flows or hard collateral have historically shown lower mark-to-market volatility than corporate credit in stress environments, but liquidity freezes can affect all private debt strategies. Stress correlations across sub-strategies, and with other illiquid asset classes, are typically higher than normalised data suggests, and mark-to-model valuation can delay recognition of losses precisely when timely risk management matters most.

Q4. What portfolio implementation or governance capabilities need to be considered?

As well as risk tolerance, this requires an assessment of illiquidity tolerance and appetite for complexity – not as a theoretical matter but as a practical one. Operational capability, reporting infrastructure and governance bandwidth are real constraints that vary significantly across institutions. For more esoteric strategies such as royalty finance or significant risk transfer, specialist due diligence capability may be a prerequisite rather than an advantage. Return dispersion across managers in some sub-strategies can be quite stark; capturing a market premium requires the right skills, and identifying the right manager is key.

Investors should also consider the composition of their existing private debt exposure. A portfolio built around 2020–2022, when rates were near zero and covenant discipline had loosened, carries a materially different risk profile to new allocations made today. Managing legacy vintage exposure and sizing new commitments are not the same exercise, and conflating them can lead to unintended concentration in the part of the cycle most exposed to current default stress.

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Q5. What premia are being harvested and is there sufficient compensation?

This returns to the nature of the premia each strategy incorporates (discussed earlier). Most private debt strategies include some form of illiquidity premium, but complexity, duration and strategy-specific premia (such as the IP premium in royalty finance or the structural premium in subordinated debt) may also be relevant. The question is whether the compensation on offer is sufficient for the specific combination of premia being assumed, particularly in an environment where some of those premia may have compressed.

Together, these questions give investors a structured basis for matching strategy to objective, and for making that choice by design rather than by default.

The matrix below maps the full strategy universe against these dimensions, offering a structured starting point for strategy selection. Assessments are indicative and characteristics may differ by individual strategy.

Private Debt – Strategy Matrix: Highest to lowest risk

Strategy	Portfolio Role	Liquidity	Complexity	Downside Protection	Macro Sensitivity	Embedded Leverage
Opportunistic & Distressed Credit						
Multi-Strategy Opportunistic	Opportunistic return	Amber	Red	Amber	Red	Red
Non-Performing Loans (NPL)	Crisis & recovery exposure	Amber	Red	Amber	Red	Amber
Special Situations	Opportunistic return Crisis & recovery exposure	Amber	Red	Amber	Red	Amber
Stressed & Distressed Loans	Cyclical high carry Crisis & recovery exposure	Amber	Red	Amber	Red	Amber
Corporate Private Credit						
Venture Debt	Cyclical high carry	Amber	Red	Red	Red	Green
Mezzanine & Subordinated Debt	Cyclical high carry	Red	Amber	Red	Red	Red
Senior / Unitranche Direct Lending	Floating-rate income	Amber	Amber	Green	Amber	Amber
Asset-Backed Finance						
Intangibles ABF (Royalties, IP, Software)	Diversifying carry	Amber	Red	Amber	Green	Amber
Significant Risk Transfer (SRT)	Diversifying carry	Red	Red	Amber	Amber	Amber
Tangibles ABF (Aircraft, Shipping, Equipment)	Diversifying carry	Amber	Amber	Green	Amber	Amber
Real Asset Debt						
NAV & Fund Finance	Liquidity solutions Floating-rate income	Green	Amber	Amber	Green	Green
Real Estate Private Debt	Defensive income	Red	Green	Green	Amber	Amber
Infrastructure Debt	Liability-aware income Defensive income	Red	Amber	Green	Green	Green

*Higher Risk

Lower Risk

Liquidity: Green = < 1 yr | Amber = 2-5 yrs | Red = 5+ yrs
 Downside protection: Green = Low | Amber = Medium | Red = High
 Embedded Leverage: Green = Low | Amber = Moderate | Red = High
 Complexity: Green = Low | Amber = Medium | Red = High
 Macro Sensitivity: Green = Low | Amber = Medium | Red = High
 *Risk ranking is indicative and may vary by individual strategy and market environment

Source: RBC Global Asset Management, May 2026.
 All Red-Amber-Green codings are indicative assessments for illustrative purposes only. Not investment advice.

The time for a more deliberate approach

Private debt has become a mainstream component of institutional portfolios, but the way most investors hold it has not kept pace with the asset class's evolution. A concentration in senior secured private credit made sense when that strategy offered a clear and well-compensated premium over public credit.

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In 2026, that proposition is more nuanced: spreads have compressed, defaults are rising from their post-pandemic lows, and renewed bank competition is adding pressure in the segment of the market that attracted most of the inflows.

The private debt opportunity set is broader than most allocations reflect

Infrastructure debt, real estate private debt, asset-backed finance across both tangibles and intangibles, and fund finance strategies each offer return drivers, collateral bases, and risk profiles that are distinct from corporate direct lending. They are not simply more of the same, and for portfolios that have been building private debt exposure for a decade primarily through one lens, they may represent a meaningful source of diversification that is currently under-utilised.

The right answer is not the same for every investor

For a pension fund seeking long-duration income with liability-matching characteristics, infrastructure debt and real estate private debt offer fixed-rate, collateral-backed cash flows that direct lending cannot replicate.

For an insurer managing Solvency II capital efficiency, the capital treatment of qualifying infrastructure and senior secured real estate debt makes strategy selection a return-on-capital question, not just a yield question.

For an endowment or foundation targeting return enhancement with a long horizon and higher complexity tolerance, asset-backed finance strategies (including royalties, IP-backed lending and significant risk transfer) offer idiosyncratic premia that are structurally uncorrelated with the corporate credit cycle.

What these three investors share is a **need for a framework rather than a shortlist**. The five diagnostic questions we have proposed portfolio role, underlying risk drivers, stress behaviour, governance capability, and premium being harvested are designed to provide that framework.

A diverse toolkit with distinct building blocks, each serving a specific purpose

The investors best positioned for that phase are those who start asking the harder questions now, not which private debt strategy is available, but which one belongs in their portfolio, and why.

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